



U.S. HOUSE OF REPRESENTATIVES
COMMITTEE ON ENERGY AND COMMERCE

May 6, 2019

TO: Republican Members, Subcommittee on Consumer Protection and Commerce

FROM: Republican Committee Staff

RE: Hearing entitled “Oversight of the Federal Trade Commission: Strengthening Protections for Americans’ Privacy and Data Security.” May 8, 2019 at 10:30 a.m. in 2123 Rayburn House Office Building.

I. REPUBLICAN PRIVACY PRINCIPLES

Any federal privacy bill must:

- **Establish One National Standard** to ensure the internet is regulated uniformly, rather than on a state-by-state basis, to provide consumers across the country (rural communities and big cities alike) the same options, opportunities, and experiences online;
- **Increase Transparency and Accountability** to ensure consumers have a better understanding of how their information is collected, used, and shared; and to ensure companies who misuse consumer information are held sufficiently accountable;
- **Protect Small Businesses and Innovation** to ensure companies, no matter the size of their compliance department, can continue to innovate and compete; and,
- **Enhance Data Security** to ensure companies have reasonable practices in place to protect consumer information.

II. WITNESSES

- The Honorable Joseph J. Simons, Chairman, Federal Trade Commission;
- The Honorable Noah Joshua Phillips, Commissioner, Federal Trade Commission;
- The Honorable Rohit Chopra, Commissioner, Federal Trade Commission;
- The Honorable Rebecca Kelly Slaughter, Commissioner, Federal Trade Commission; and,

- The Honorable Christine S. Wilson, Commissioner, Federal Trade Commission.

III. BACKGROUND

The Federal Trade Commission (FTC or Commission) is an independent agency that was established by Congress in 1914, through the Federal Trade Commission Act of 1914 (FTC Act).¹ As the successor to the Bureau of Corporations, the agency's original mission was to prevent "[u]nfair methods of competition,"² and expanded in 1938 to include "unfair or deceptive acts or practices in or affecting commerce."³ The FTC performs its dual mission to promote competition and protect consumers by preventing anti-competitive, deceptive, and unfair business practices through civil law enforcement, injunctive relief, investigations, advocacy, and education.

The Commission enforces a variety of laws, including the Fair Credit Reporting Act, the Clayton Act, the Gramm-Leach-Bliley Act (GLBA), the Children's Online Privacy Protection Act, the Controlling the Assault of Non-Solicited Pornography and Marketing Act, the Do-Not-Call Implementation Act, and the Dodd-Frank Wall Street Reform and Consumer Protection Act.⁴ The FTC also enforces various rules issued pursuant to the FTC Act or the aforementioned laws, including the GLBA Safeguards Rule and Telemarketing Sales Rule. In total, the FTC has administrative and enforcement responsibilities under more than 70 laws (over 50 of which have a consumer protection purpose).⁵

The FTC is headed by a five-member Commission, nominated by the President, and confirmed by the United States Senate, with each member serving a staggered seven-year term.⁶ Not more than three Commissioners may be affiliated with the same political party. The President designates one Commissioner to serve as Chairman of the Commission. The activities and actions of the FTC are carried out by the Bureaus of Competition (BC), Consumer Protection (BCP), and Economics (BE), and supported by various offices and eight regional offices across the country.⁷

The FTC Fiscal Year 2020 budget request has a program level of \$312.3 million and 1,140 full-time equivalents (FTEs).⁸ The FY 2020 request constitutes an overall increase of about \$5.9 million above the annualized amount provided to the FTC in the FY 2019 continuing resolution and consists of the following: approximately \$1.4 million for BCP to refresh the Tech Lab, which provides staff with the technological tools to conduct effectively investigations and research in support of the FTC's consumer protection mission; approximately \$1.6 million for

¹ Federal Trade Act of 1914, *as amended*, 38 Stat. 717, 15 U.S.C. § 41 (2018).

² 15 U.S.C. § 45(a)(1) (2018).

³ *Id.*

⁴ <https://www.ftc.gov/enforcement/statutes>

⁵ *Id.*

⁶ <https://www.ftc.gov/about-ftc/commissioners>

⁷ <https://www.ftc.gov/about-ftc/bureaus-offices>

⁸ https://www.ftc.gov/system/files/documents/reports/fy-2020-congressional-budget-justification/fy_2020_cbj.pdf

BC's expert witness needs due to increased numbers of complex investigations and litigations; and \$3 million for the Office of the Executive Director for IT modernization.⁹

A. Consumer Protection

i. Unfair or Deceptive Acts or Practices and Enforcement

15 U.S.C. § 45(a)(1), more commonly referred to as Section 5, makes “unfair or deceptive acts or practices in or affecting commerce” unlawful.¹⁰ Pursuant to § 45(a)(2), the FTC is empowered to prevent persons, partnerships, or corporations from “using unfair or deceptive acts or practices in or affecting commerce.”¹¹ An act or practice is “unfair” if it causes, or is likely to cause, substantial injury not reasonably avoidable by consumers and not outweighed by countervailing benefits to consumers or competition as a result of the practice.¹² An act or practice is “deceptive” if it is material and is likely to mislead consumers acting reasonably under the circumstances.¹³

Following an investigation, the Commission may initiate an enforcement action if it “has reason to believe” that the law is being or has been violated.¹⁴ Specifically, “[w]henver the Commission shall have reason to believe that any such person, partnership, or corporation has been or is using...any unfair or deceptive act or practice in or affecting commerce” and if an action “would be in the interest of the public” the FTC is to bring such an action.¹⁵ If the FTC decides to bring an action, the FTC may bring an administrative action, apply a trade regulation rule, or seek judicial intervention.

Under Section 5(b) of the FTC Act (15 U.S.C. § 45(b)), the Commission may challenge violations through an administrative adjudication by issuing a complaint and either settling with the respondent or, if the respondent challenges the charges in the complaint, adjudicate such complaint before an administrative law judge. The Commission, if successful, enters a final order and, if the party violates the terms of that order, the Commission may seek civil penalties.¹⁶

The Commission may use trade regulation rules to remedy violations that occur on an industry-wide basis. Specifically, under Section 18 of the FTC Act (15 U.S.C. § 57a), the Commission can prescribe “rules which define with specificity acts or practices which are unfair or deceptive” and once the Commission has promulgated a trade regulation rule, anyone who “with actual knowledge or knowledge fairly implied on the basis of objective circumstances that such act is unfair or deceptive and is prohibited by” a rule is subject to civil penalties.¹⁷ Additionally, any person who violates a promulgated rule is liable for injury caused to

⁹ *Id.*

¹⁰ 15 U.S.C. § 45(a)(1)

¹¹ 15 U.S.C. § 45(a)(2)

¹² <https://www.gao.gov/assets/700/696437.pdf> at 9.

¹³ *Id.*

¹⁴ 15 U.S.C. § 45(b)

¹⁵ *Id.*

¹⁶ <https://www.ftc.gov/about-ftc/what-we-do/enforcement-authority>

¹⁷ *Id.*

consumers and the Commission may pursue consumer redress.¹⁸ In total, the Commission has returned more than \$2.3 billion in refunds to consumers.¹⁹ In its most recent report, which covers July 2017 to June 2018, the Commission returned a total \$122 million.²⁰

If the Commission decides to go through an adjudication or finds that a trade regulation applies, the Commission must still seek aid of a court to obtain civil penalties or consumer redress.²¹ The FTC can also challenge an act or practice directly in court without any prior agency determination. Under Section 13(b) of the FTC Act (15 U.S.C. § 53(b)), the Commission may seek a preliminary and permanent injunction if the Commission has “reason to believe” that a party is violating any provision of the Act.²²

Section 13(b) allows the FTC to ask the court to enjoin the allegedly unlawful conduct pending completion of the FTC administrative proceeding to determine whether the conduct is in fact unlawful. Originally, this authority was to be used principally against corporate acquisitions, but in the 1970s and 1980s, the FTC began to expand its use in its consumer protection efforts to challenge fraud and deception cases.²³ Recently, such expanded use has been called into question. Last year, in *FTC v. Shire ViroPharma, Inc.*, the Third Circuit Court of Appeals held that the Commission cannot seek an injunction and restitution under Section 13(b) against a company in federal court over alleged past conduct absent an allegation, supported by evidence, that the company is violating or is about to violate the law again.²⁴

ii. Historical Perspective: Rulemaking at the FTC

In 1964, the FTC set forth three factors to consider when deciding whether to wield its unfairness authority: whether an act or practice 1) caused substantial injury to consumers, competitors, or other businesses; 2) offended public policy; and 3) was immoral, unethical, or unscrupulous.²⁵ In 1972, in *FTC v. Sperry & Hutchinson*, 405 U.S. 223 (1972), the Supreme Court cited these factors *in dicta* and in 1975, Congress enacted the Magnuson-Moss Act, which confirmed the authority of the Commission to enact substantive rules under Section 5 of the FTC Act. However, as former Chairman Timothy J. Muris explained, these events enabled the Commission to enact trade regulations rules which amounted to “legislat[ing] before the fact instead of having to proceed case by case against individual businesses.”²⁶

¹⁸ *Id.*

¹⁹ https://www.ftc.gov/system/files/documents/reports/2018-annual-report-refunds-consumers/annual_redress_report_2018.pdf

²⁰ *Id.*

²¹ <https://www.ftc.gov/about-ftc/what-we-do/enforcement-authority>

²² *Id.*

²³ *Id.*

²⁴ <https://www2.ca3.uscourts.gov/opinarch/181807p.pdf> at 5. The Commission argued that the phrase “is violating or is about to violate” in Section 13(b) is “satisfied by showing a past violation and a reasonable likelihood of recurrent future conduct.”²⁴ Ruling against the Commission, the Third Circuit concluded that the language in Section 13(b) is “unambiguous” and that it “prohibits existing or impending conduct.”

²⁵ <http://media.ca11.uscourts.gov/opinions/pub/files/201616270.pdf> at 11.

²⁶ <https://www.aei.org/publication/rules-without-reason-the-case-of-the-ftc/print/>

Following the *Sperry & Hutchinson* decision and enactment of the Magnuson-Moss Act, the Commission “set forth to test the limits of its unfairness doctrine.”²⁷ Over the next 15 months, the Commission initiated a rule a month, “usually without a clear theory...[and] with only a tenuous connection between the perceived problem and the recommended remedy, and with, at best, a shaky empirical foundation.”²⁸ According to former Chairman Muris, “the Commission had sought to become the second most powerful legislature in Washington” and “in the 1970s...embarked on a vast enterprise to transform entire industries.”²⁹

In 1978, the problem of overreach by the Commission culminated with FTC’s desire to ban all advertising to children, arguing that it satisfied its third unfairness factor: that advertising to children was an act or practice that was immoral, unscrupulous, and unethical. The Commission’s action led to the Washington Post editorial headline: “The FTC as the National Nanny.”³⁰ According to the article, the decision to impose these restrictions was “a preposterous intervention that would turn the agency into a great national nanny.” Congress and much of the public did not approve.³¹ For a short period of time, Congress refused to fund the FTC which shut the Commission down for several days.³²

In 1980, Congress enacted the Federal Trade Commission Improvements Act (also referred to as Magnuson-Moss), which prevented the Commission from using unfairness in new rulemakings to restrict advertising and placed more obligations on the Commission for other new rules.³³

iii. LabMD

In 2013, the FTC issued an administrative complaint against LabMD, a now-closed small medical laboratory that employed about 30 people and conducted cancer diagnostic testing, for allegedly lacking reasonable data security practices.

LabMD was forced to shutter its operation because a company exfiltrated a file from their system, used that file to first pressure the company to hire them and then, when rebuffed, sought government action, which forced LabMD to undergo years of investigations and litigation, only for a court to determine the government action itself was not enforceable. The LabMD case highlights the real-world impact of government intervention. The case arises from the following facts:

²⁷ <http://media.ca11.uscourts.gov/opinions/pub/files/201616270.pdf> at 11; see also J. Howard Beales, *The FTC’s Use of Unfairness Authority: Its Rise, Fall, and Resurrection*, FTC (May 30, 2003), <https://www.ftc.gov/public-statements/2003/05/ftcs-use-unfairness-authority-its-rise-fall-and-resurrection>

²⁸ https://www.law.gmu.edu/assets/files/publications/working_papers/1617.pdf at 1.

²⁹ *Id.*

³⁰ https://www.washingtonpost.com/archive/politics/1978/03/01/the-ftc-as-national-nanny/69f778f5-8407-4df0-b0e9-7f1f8e826b3b/?noredirect=on&utm_term=.638218d3c090

³¹ *Id.*

³² <https://www.ftc.gov/public-statements/2003/05/ftcs-use-unfairness-authority-its-rise-fall-and-resurrection>

³³ <https://www.iab.com/news/privacy-ftc-rulemaking-authority-a-historical-context/>

- In 2008, Tiversa Holding Corporation, an entity specialized in data security, acquired³⁴ a file containing personal information from LabMD through the peer-to-peer file sharing application, LimeWire.³⁵
- Tiversa subsequently contacted LabMD to sell its remediation services to protect against persons from acquiring the file Tiversa extracted from LabMD. LabMD refused.³⁶
- Tiversa had been communicating with the FTC about the information, but because Tiversa had also solicited LabMD to acquire their services, Tiversa did not want the FTC to issue a Civil Investigative Demand (CID) on Tiversa.³⁷
- Tiversa created a separate entity, The Privacy Institute, and in 2009, made arrangements with the FTC to issue a CID on The Privacy Institute. As a result, The Privacy Institute provided the FTC the file it pulled from and used to acquire business from LabMD.³⁸

Following an investigation, the Commission issued an administrative complaint against LabMD alleging that LabMD had violated Section 5(a) of the FTC Act by “engaging in a number of practices that, taken together, failed to provide reasonable and appropriate security for personal information on its computer networks.”³⁹ However, rather than allege specific acts or practices that were unfair, the Commission laid out allegations of what LabMD failed to do.

An administrative law judge (ALJ) originally dismissed the Commission’s complaint, but the FTC reversed the ALJ’s decision, finding LabMD had failed to implement reasonable security measures. The Commission entered an order vacating the ALJ’s decision and enjoining LabMD to create and implement a variety of data security measures. LabMD appealed the FTC’s decision, petitioning the Eleventh Circuit Court of Appeals to vacate the Commission’s order, arguing the “order [was] unenforceable because it [did] not direct LabMD to cease committing an unfair act or practice within the meaning of Section 5(a).”⁴⁰

In 2018, the Eleventh Circuit agreed and vacated the Commission’s order.⁴¹ The Court did so because it “contain[ed] no prohibitions,” but rather “command[ed] LabMD to overhaul and replace its data-security program to meet an indeterminable standard of reasonableness” and, therefore, the Court found the “command unenforceable.”⁴²

³⁴ Notably, it was never shown that anyone other than Tiversa accessed the data or that any misuse was made of the data.

³⁵ <http://media.ca11.uscourts.gov/opinions/pub/files/201616270.pdf> at 3.

³⁶ *Id.* at 4.

³⁷ *Id.*

³⁸ *Id.*

³⁹ *Id.* at 5.

⁴⁰ <http://media.ca11.uscourts.gov/opinions/pub/files/201616270.pdf> at 2.

⁴¹ *Id.* at 31.

⁴² *Id.* at 27.

B. The Commission's Efforts on Privacy

The FTC is the primary law enforcement agency charged with preventing the majority of commerce from using unfair or deceptive acts or practices. The FTC has applied its Section 5 authority where deceptions or violations of written privacy policies and representations of data security have occurred. As of December 2018, the FTC has brought enforcement actions addressing a number privacy and data security issues, which includes over 130 spam and spyware cases, 75 general privacy lawsuits, 65 data security cases, almost 30 cases under Gramm-Leach-Bliley Act (GLBA), and 25 cases under Children's Online Privacy Protection Act (COPPA).⁴³ COPPA is an example of a statute that granted the FTC limited rulemaking authority outside of the Magnuson-Moss updates.

FTC actions generally result in a settlement where the parties agree to terms laid out in a consent decree. These settlement agreements typically require a company to: implement reasonable privacy and security programs; subject the company to long-term monitoring of compliance, in almost all cases 20 years; provide monetary redress to consumers where applicable; forfeit any money gained from the unfair or deceptive conduct; delete illegally obtained consumer information; and provide increased transparency and choice mechanisms to consumers.⁴⁴ If a company violates the terms of the consent decree, the FTC can seek judicial enforcement to levy civil penalties.⁴⁵

i. 2012 Report: "Protecting Consumer Privacy in an Era of Rapid Change"

In 2012, the FTC published a report, "Protecting Consumer Privacy in an Era of Rapid Change," to provide recommendations for businesses and policymakers.⁴⁶ In this report, the FTC provides the following implementation recommendations:

- **Scope:** The framework applies to all commercial entities that collect or use consumer data that can be reasonably linked to a specific consumer, computer, or other device, unless the entity collects only nonsensitive data from fewer than 5,000⁴⁷ consumers per year and does not share the data with third parties.⁴⁸

⁴³ <https://www.ftc.gov/system/files/documents/reports/privacy-data-security-update-2018/2018-privacy-data-security-report-508.pdf>

⁴⁴ <https://www.gao.gov/assets/700/696437.pdf> at 10.

⁴⁵ *Id.*

⁴⁶ <https://www.ftc.gov/sites/default/files/documents/reports/federal-trade-commission-report-protecting-consumer-privacy-era-rapid-change-recommendations/120326privacyreport.pdf>

⁴⁷ To address concerns about undue burdens on small businesses, the final framework does not apply to companies that collect only non-sensitive data from fewer than 5,000 consumers a year, provided they do not share the data with third parties.

⁴⁸ *Id.* at 7.

- **Privacy by Design:** The Commission recommends companies promote consumer privacy throughout their organizations and at every stage of the development of their products and services.⁴⁹
- **Simplify Consumer Choice:** The Commission recommends companies simplify choice by implementing practices that do not require choice or, where companies do offer a choice, such choice should be offered at a time and in a context in which the consumer is making a decision about his or her data.⁵⁰
- **Transparency:** The Commission recommends companies implement clearer, shorter, and more standardized privacy notices; controls to allow consumers access to their data; and better educate consumers about commercial data privacy practices.⁵¹

The FTC is currently conducting a series of workshops on issues within its jurisdiction, several focusing on consumer protection issues, including privacy and data security (“Hearings on Competition and Consumer Protection in the 21st Century”).⁵²

C. Energy and Commerce Activity

i. 115th Oversight Hearing

On July 18, 2018, the Digital Commerce and Consumer Protection Subcommittee held a hearing with the Commission entitled “Oversight of the Federal Trade Commission.” The focus of the hearing, among other items, was the FTC’s budget, mission, performance, and authorities; the FTC’s priorities and efforts with respect to issues including robocalls, data security, and privacy; and the FTC’s role in the Privacy Shield review with the European Union.⁵³ At the time, the following Commissioners were at the Commission and testified before the Subcommittee: Chairman Simons and Commissioners Ohlhausen, Phillips, Chopra, and Slaughter.⁵⁴

ii. FTC Process Reform Efforts

The FTC’s consumer protection mandate to enjoin “unfair or deceptive acts or practices in or affecting commerce”⁵⁵ is a flexible framework that has allowed new, emerging technologies to progress without prior regulatory permission. However, the FTC settles most of its consumer protection cases,⁵⁶ especially in areas involving newer technologies such as data security.⁵⁷

⁴⁹ *Id.*

⁵⁰ *Id.* at 7-8.

⁵¹ *Id.* at 8.

⁵² <https://www.ftc.gov/policy/hearings-competition-consumer-protection>

⁵³ <https://docs.house.gov/meetings/IF/IF17/20180718/108560/HHRG-115-IF17-20180718-SD002.pdf>

⁵⁴ *Id.*

⁵⁵ 15 U.S.C. § 45(a)(1).

⁵⁶ <https://www.ftc.gov/enforcement/cases-proceedings>

⁵⁷ Out of 62 data security cases listed on the FTC’s website, the only two defendants that have not settled are LabMD, Inc. and Wyndham Worldwide Corporation. See <https://www.ftc.gov/enforcement/cases-proceedings/terms/249>.

Settling a high percentage of cases avoids costly litigation but carries risks in terms of appropriate cost-benefit analysis and offering certainty to industry for investment and innovation.⁵⁸ Over the years, the Energy and Commerce Committee considered a number of bills to amend FTC processes and protect data security.

The bills helped ensure that the FTC's framework appropriately balanced consumer protection with safeguarding innovations that may pose theoretical risks but have not led to concrete harm. Eight of the bills made targeted amendments to the FTC's processes and helped provide transparency as it carries out its consumer protection mission under Section 5 of the FTC Act. The bills were designed to help companies better predict their liability under Section 5 to facilitate and encourage innovative product and service development for consumers. The following bills were reported out of Committee:

- H.R. 5093, Technological Innovation through Modernizing Enforcement (TIME) Act: limited consent orders to expire not later than eight years;
- H.R. 5118, the Solidifying Habitual and Institutional Explanations of Liability and Defenses (SHIELD) Act: clarified that in any enforcement action, the Commission must prove a violation of a provision of law enforced by the FTC.
- H.R. 5097, Start Taking Action on Lingering Liabilities Act (STALL): required the Commission to terminate an investigation after six months unless the Commission votes to extend the investigation.
- H.R. 5136, Revealing Economic Conclusions for Suggestions (RECS) Act: prohibited the Commission from submitting recommendations for legislative or regulatory action without an economic analysis by the Bureau of Economics.
- H.R. 5109, Clarifying Legality and Enforcement Action Reasoning (CLEAR) Act: required the Commission to submit an annual report to Congress on investigations relating to unfair or deceptive acts or practices.
- H.R. 5115, Statement on Unfairness Reinforcement and Emphasis Act (SURE Act): clarified that an act or practice does not cause substantial injury to consumers if the injury or harm is trivial or merely speculative.
- H.R. 5116, Freeing Responsible and Effective Exchanges (FREE) Act: authorized a bipartisan majority of FTC Commissioners to hold a non-public meeting if no votes or agency actions were taken, each person was a Commissioner or

⁵⁸ See Gerard Stegmaier & Wendell Bartnick, *Essay: Psychics, Russian Roulette, and Data Security: The FTC's Hidden Data-Security Requirements*, 20 GEO. MASON L. REV. 673, 693 (2013) ("It is unclear whether nonparties to the investigation should attempt to follow the complaint, the consent order, or both when complying with Section 5, or whether the failure to implement some or all of the measures would result in a prohibited unfair practice.").

employee of the Commission, and an attorney from the Office of General Counsel of the Commission is present.

- H.R. 5098, FTC Robust Elderly Protections and Organizational Requirements to Track Scams (REPORTS) Act: required the Commission to publish and submit to Congress an annual plan.
- H.R. 5255, to amend the Federal Trade Commission Act to permit the Federal Trade Commission to enforce such Act against certain tax-exempt organizations.
- H.R. 1770, requires certain commercial entities that use personal information to:
(1) implement security measures to protect electronic information against unauthorized access and acquisition; (2) restore the integrity, security, and confidentiality of their data systems following the discovery of a security breach; and (3) determine whether there is a risk that a breach will result in identity theft, economic loss or harm, or financial fraud to individuals' personal information.

III. STAFF CONTACTS

Please contact Melissa Froelich or Bijan (BJ) Koohmaraie of the Republican Committee staff at (202) 225-3641 with questions.